

lowest qualified bench mark for an equity option with standardized terms on the same stock having the same applicable stock price.

(ii) *Examples.* The following examples illustrate the rules set out in paragraph (c)(2)(i) of this section:

Example 1. Taxpayer owns stock in Corporation X. Taxpayer writes an equity call option with flexible terms on Corporation X stock through a national securities exchange for a term of not more than 12 months. The applicable stock price for Corporation X stock is \$73.75. Using the bench marks for an equity option with standardized terms with an applicable stock price of \$73.75, the highest available strike price less than the applicable stock price is \$70, and the second highest strike price less than the applicable stock price is \$65. Therefore, an equity call option with flexible terms on Corporation X stock with a term of 90 days or less will not be deep in the money if the strike price is not less than \$70. If the term is greater than 90 days, an equity call option with flexible terms on Corporation X will not be deep in the money if the strike price is not less than \$65.

Example 2. Taxpayer owns stock in Corporation Y. Taxpayer writes a 9-month equity call option with flexible terms on Corporation Y stock through a national securities exchange. The applicable stock price for Corporation Y stock is \$14.75. Using the bench marks for an equity option with standardized terms with an applicable stock price of \$14.75, the highest available strike price less than the applicable stock price is \$12.50. However, under section 1092(c)(4)(D), the lowest qualified bench mark can be no lower than 85% of the applicable stock price, which for Corporation Y stock is \$12.54. Thus, because the highest available strike price less than the applicable stock price for an equity option with standardized terms is lower than the lowest qualified bench mark under section 1092(c)(4)(D), the lowest strike price at which a qualified covered call option can be written is the next higher strike price, or \$15.00. This \$15.00 strike price requirement for a qualified covered call option applies to equity options with flexible terms, equity options with standardized terms, and qualifying over-the-counter options.

Example 3. Taxpayer owns stock in Corporation Z. On May 8, 2003, Taxpayer writes a 21-month equity call option with flexible terms on Corporation Z stock through a national securities exchange. The applicable stock price for Corporation Z stock is \$100. The bench marks for a 21-month equity option with standardized terms with an applicable stock price of \$100 will be based upon the adjusted applicable stock price. Using the table at § 1.1092(c)-4(e), the applicable

stock price of \$100 is multiplied by the adjustment factor 1.12, resulting in an adjusted applicable stock price of \$112. The highest available strike price less than the adjusted applicable stock price is \$110, and the second highest strike price less than the adjusted applicable stock price is \$105. Therefore, a 21-month equity call option with flexible terms on Corporation Z stock will not be deep in the money if the strike price is not less than \$105.

(d) *Effective date*—(1) *In general.* Except as provided in paragraph (d)(2) of this section, this section applies to equity options with flexible terms entered into on or after January 25, 2000.

(2) *Effective date for paragraphs (b) and (c) of this section.* Paragraphs (b) and (c) of this section apply to equity options with flexible terms entered into on or after July 29, 2002.

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§ 1.1092(c)-3 Qualifying over-the-counter options.

(a) *In general.* Under section 1092(c)(4)(B)(i), an equity option is not a qualified covered call option unless it is traded on a national securities exchange that is registered with the Securities and Exchange Commission or other market that the Secretary determines has rules adequate to carry out the purposes of section 1092(c)(4). In accordance with section 1092(c)(4)(H), this requirement is modified as provided in paragraph (b) of this section.

(b) *Qualified covered call option status.* A qualifying over-the-counter option, as defined in § 1.1092(c)-4(c), is a qualified covered call option if it meets the requirements of §§ 1.1092(c)-1 and 1.1092(c)-2(c) after using the language “qualifying over-the-counter option” in place of “equity option with flexible terms”. For purposes of this paragraph (b), a qualifying over-the-counter option is deemed to satisfy the requirements of section 1092(c)(4)(B)(i).

(c) *Effective date.* This section applies to qualifying over-the-counter options entered into on or after July 29, 2002.

[67 FR 20900, Apr. 29, 2002]

§ 1.1092(c)-4 Definitions.

The following definitions apply for purposes of §§ 1.1092(c)-1 through 1.1092(c)-3: